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No. 552

In the

Supreme Court of the United States

October Term, 1961

ESTATE OF LEO M. GARTLAND, Deceased,
MATTHEW GARTLAND, Administrator,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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In the

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COMMISSIONER OF INTERNAL REVENUE
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

TO THE HONORABLE CHIEF JUSTICE AND ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Petitioner, Estate of Leo M. Gartland, Deceased, Mat thew Gartland, Administrator, prays that a Writ of Certiorari issue to review the Judgment of the Court of Appeals, Seventh Circuit, entered August 4, 1961, and Application for Rehearing denied September 7, 1961.

OPINIONS BELOW

The Opinion of the Court of Appeals is reported at —— F.2d, ——; 8 AFTR 2 145707. The Opinion of the Tax Court of the United States is reported at 34 T.C., No. 89.

BASIS OF JURISDICTION

The jurisdiction of this Court rests on 28 U.S.C., 1254 (1).

QUESTION PRESENTED

Decedent's father created a Trust in 1929, giving the Trustee discretion to pay decedent income during his life and, upon his death, income to his widow and, at her death, the trust corpus and accumulated income to his children. Decedent was given power to amend the Trust or to terminate the Trust. Upon termination of the Trust, decedent was to receive the corpus and accumulated income. On May 16, 1931, decedent asked the Trustee to send him all of the income. On January 19, 1938, decedent executed a formal document, asking that all income be sent to him. On June 20, 1945, decedent executed a document releasing his power of appointment. This release was executed pursuant to the provisions of the Revenue Act of 1942, giving possessors of power of appointment the privilege to release such power without subjecting such a release to tax. Decedent died intestate on April 1, 1955, survived by his widow and three children, who claimed their interest under the Trust Agreement created by decedent's father in 1929. The respondent contended that the action of the decedent was equivalent to the exercise of the power taking the entire Estate, keeping the income, and leaving the corpus to the widow for life and to his children thereafter as a disposition of the

type described in Sections 2041(A)(1)(B) and 2036 of the Internal Revenue Code of 1954.

STATUTES INVOLVED

Internal Revenue Code of 1954, c.736, 68A Stat. 382 and 385

"Sec. 2041. Powers of Appointment

(a) In General.—The value of the gross estate shall include the value of all property (except real property situated outside of the United States)—

(1) Powers of appointment created on or before October 21, 1942.—To the extent of any property with respect to which a general power of appointment created on or before October 21, 1942, is exercised by the decedent—

* * *

(B) by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includable in the decedent's gross estate under sections 2035 to 2038, inclusive;

but the failure to exercise such a power or the complete release of such a power shall not be deemed an exercise thereof."

"Sec. 2036. Transfers with retained life estate.

(a) General Rule.—The value of the gross estate shall include the value of all property (except real property situated outside of the United States) to the extent of any interest therein of which the decedent has at any time made a transfer (except in case of a bona fide sale for an adequate and full consideration in money or money's worth), by trust or otherwise, under which he has retained for his

life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death—

(1) the possession or enjoyment of, or the right to the income from, the property, or

(2) the right, either alone or in conjunction with any person, to designate the persons who shall possess or enjoy the property or the income therefrom."

Prior to September 1, 1959, Section 16 of the New York Personal Property Law provided as follows:

"An accumulation of the income of personal property, directed by any instrument sufficient in law to pass such property is valid:

1. If directed to commence from the date of the instrument, or the death of the person executing the same, and to be made for the benefit of one or more minors then in being, or in being at such death, and to terminate at or before the expiration of their minority.

2. If directed to commence at any period subsequent to the date of the instrument or subsequent to the death of the person executing it, and directed to commence within the time allowed for the suspension of the absolute ownership of personal property, and at some time during the minority of the persons for whose benefit it is intended, and to terminate at or before the expiration of their minority.

3. All other directions for the accumulation of the income of personal property, not authorized by statute, are void. In either case mentioned in subdivisions one and two of this section, a direction for any such accumulation for a longer term than the minority of the persons intended to be benefited thereby, has the same effect as if limited to the

minority of such persons, and is void as respects the time beyond such minority."

Repealed N.Y. Sess. Laws 1959, c. 453, § 1, 4, effective Sept. 1, 1959.

STATEMENT OF MATERIAL FACTS

Leo M. Gartland died intestate on April 1, 1955, survived by his widow and three children, one of whom is the petitioner, Matthew Gartland, Administrator of the Estate of Leo M. Gartland. Petitioner, as Administrator, filed the estate tax return on June 12, 1956 with the District Director of Internal Revenue in Indianapolis, Indiana (A-21-2).

On July 10, 1929, decedent's father, Matthew F. Gartland, of Marion, Indiana, transferred certain assets to S. Roswell Shepherd, of West Orange, New Jersey, as trustee under a trust agreement. On July 18, 1929, S. Roswell Shepherd acknowledged delivery of the trust agreement in Jersey City, New Jersey, and accepted the trusteeship. On July 23, 1929, S. Roswell Shepherd, under the authority granted to him by the trust instrument, appointed the National City Bank of New York as co-trustee and the Farmers Loan and Trust Company as successor trustee, if the appointed co-trustee should resign. The National City Bank of New York accepted the appointment and, on August 6, 1929, S. Roswell Shepherd resigned as co-trustee. On January 20, 1930, the National City Bank of New York resigned as trustee and the City Bank Farmers Trust Company, successor to the Farmers Loan and Trust Company, accepted appointment as successor trustee. There were no further changes in trustees and at decedent's death the City Bank Farmers Trust Company was acting as successor trustee (A-22-3).

Subdivision A of Article 1 of the trust agreement provided as follows:

> "1. In disposing of the income and principal of this trust the Trustee's duties shall be:
>
> "A. To pay over to my son, Leo M. Gartland, so much of the income as the Trustee in his discretion shall deem advisable and to accumulate the remaining income and add it to the principal of the trust fund during the life of my said son.
>
> "B. Upon the death of my said son to pay over the income to my daughter-in-law, Irene S. Gartland, during her life" (A-26).

At the time of the transfer of the assets of the trust to the National City Bank of New York in 1929 and thereafter until the statute was repealed in 1959, the New York statutes on accumulation of income from personal property prohibited accumulations of such income except during the minority of a beneficiary. These statutes required that all income directed *or permitted* to be accumulated must instead be paid out currently to the income beneficiary who would take in the absence of the invalid provision. New York Personal Property Law, Section 16.

Article 8 of the trust agreement provided as follows:

> "8. I hereby authorize and empower my son, Leo M. Gartland, during his life, to amend or terminate his agreement in whole or in part and to change any beneficial interest hereunder by delivering to the trustee an instrument in writing executed by him. In the event of the termination of this trust by my said son, the trustee shall pay over the principal of the trust fund to him or to such person or persons as he may designate in writing to the trustee" (A-30).

On August 15, 1929, the decedent, pursuant to the power granted to him under paragraph 8 of the trust in-

strument, executed a document making a certain change in the trust instrument for the purpose of avoiding questions of a violation of the rules against perpetuities, and to provide specifically for the dispostion of one-half of the principal allocated to his daughters. Respondent and the Tax Court recognized that such amendment was not a sufficient exercise of the general power of appointment to be a disposition which would fall within the provisions of Section 2041(a)(1)(B) of the 1954 Code (A-22, 26).

On May 16, 1931, the decedent, by letter addressed to the City Bank Farmers Trust Company, instructed said bank, as trustee, as follows:

> "Owing to present conditions the writer finds it necessary to use the income of his Trust. You may use this as your authority to transfer the cash in my principal account to the income account and send check at your convenience. You may use these instructions until further notice" (A-32).

On May 19, 1931, in compliance with the letter, the trustee paid the decedent $1,292.98, which amount was comprised of current income of $745.63 and $547.35 of income withheld from decedent in prior years (A-23, 32-3).

On January 19, 1938, decedent executed a document addressed to the trustee, which document ratified the payment by the trustee to the decedent of the current trust income and the accumulated income which had previously been added to trust principal, and further provided:

> ". . . the said Leo M. Gartland does hereby amend said trust by striking out, canceling and annulling Subdivision "A" of Article 1 thereof and by substituting in lieu thereof a new Subdivision "A" of Article 1 which shall read as follows:
>
> 'A. To pay over the net income thereof to my son, Leo M. Gartland, during his life.'

all with the same force and effect as if this instrument had been delivered by him to said Trustee on May 16, 1931" (A-33-5).

No subsequent amendments were made and on June 20, 1945, decedent executed a document which provided as follows:

"That I do hereby finally and irrevocably renounce, release and surrender the Power of Appointment which is conferred upon me in and by Paragraph 8 of a Trust Agreement made by my father, the late Matthew F. Gartland, of Marion, Indiana dated July 10th, 1929, over the trust fund for my benefit under said trust agreement. It is my intent by this instrument to divest myself completely and irrevocably of all powers, rights and privileges granted to me by said trust agreement to dispose of, or to direct the disposition of, the principal or income of any part of the trust fund for my benefit under said trust agreement, as if such power of appointment had not been granted" (A-36).

None of the original corpus was ever paid to decedent or distributed pursuant to his directions. At the date of decedent's death, April 1, 1955, the corpus of the trust had a fair market value of $258,968.29 (A-24-5).

REASONS FOR GRANTING THE PETITION

(A) The Court of Appeals, Seventh Circuit, reached an incorrect conclusion that because petitioner took the income from the Trust during his life that it was equivalent to his taking the entire Trust, keeping the income, and leaving the balance to his widow and children.

(B) The Court of Appeals, Seventh Circuit, was likewise incorrect in the conclusion reached that decedent had no rights under the Trust Agreement to income be-

cause the Trustee, in its discretion, could give all, part, or none of the income. Its Decision was incorrect under the laws of New York in that they forbid the accumulation of income, and the effect of such a Statute is to require that all the income be distributed. The letters of the decedent asking for the income, therefore, were ineffective because the law required that such income be given to him.

(C) The request for the income by decedent, even if the laws of New York did not specifically require that such be distributed to him, was a partial exercise of the power in that it asked for the income only and could not be construed as a termination of the Trust, or a request for the entire corpus of the Trust.

(D) The release of the power of appointment by the decedent under the Revenue Act of 1942, was an exercise of a power, which Congress made not subject to tax, and the Decision of the Court of Appeals is, therefore, erroneous in subjecting the Estate to a tax by reason of such an exercise.

SUMMARY OF ARGUMENT

Neither decedent's letter of May 16, 1931, as ratified by the 1938 amendment, requesting all of the net income of his father's trust rather than "so much" as the trustee might pay to him, nor his release on June 20, 1945 of his power to amend or terminate the trust, was an "exercise" of a pre 1942 general power of appointment. By none of his acts did decedent directly or impliedly direct, or evidence an intent to direct, distribution of the property contained in his father's trust. The only thing decedent did was to take for himself the entire income for his life rather than "so much" as the trustee might pay to him, and this did not constitute an "exercise" of a pre 1942 general power of appointment. Upon decedent's

death, the trust property devolved according to the terms of the trust agreement as fixed by his father and not by any direction of decedent.

Moreover, decedent's letter, as ratified by the 1938 amendment, was a nullity because of the New York law which prohibits accumulations of income except during the minority of a beneficiary. Hence, since the New York law required the trustee to distribute the entire net income to decedent, his taking of such income did not constitute an "exercise" of a pre 1942 general power of appointment.

Even if it be assumed, however, that one or more or all of the three instruments constituted an "exercise" of a pre 1942 general power of appointment over his father's trust property, such exercise would not require the trust property to be included in decedent's gross estate because there was no disposition of the type described in Sections 2041(a)(1)(B) and 2036. Decedent did not "transfer" the trust property and "retain" for himself the income therefrom, as is required if the property is to be included in decedent's taxable estate. Decedent merely took for himself all of the income rather than "so much" as the trustee might pay to him.

CONTESTED ISSUE

Did either decedent's letter of May 16, 1931 requesting the trustee to pay him the entire income rather than such amount as the trustee might determine his amendment to the trust of January 19, 1938 ratifying this action, or his release of January 20, 1945, or any combination of them, constitute an exercise of a pre 1942 general power of appointment and if there was an exercise, was it an exercise of such a power by a disposition of the type described in Sections 2041(a)(1)(B) and 2036 of the Internal Revenue Code of 1954, c.736, 68A Stat. 382 and 385.

The 1942 Revenue Act provided that the release of a pre-1942 Power of Appointment could be made without taxable effect. The Court below has now held in effect that such a release resulted in taxability.

PROPOSITIONS OF LAW RELIED UPON

I.

NEITHER DECEDENT'S LETTER OF MAY 16, 1931 REQUESTING THE ENTIRE INCOME RATHER THAN SO MUCH AS THE TRUSTEE MIGHT DETERMINE, NOR DECEDENT'S AMENDMENT OF JANUARY 19, 1938 RATIFYING THIS ACTION, NOR HIS RELEASE ON JUNE 20, 1945 OF HIS POWER TO AMEND OR TERMINATE THE TRUST, CONSTITUTED AN EXERCISE OF A GENERAL POWER OF APPOINTMENT.

The Letter of May 16, 1931, As Ratified by the 1938 Amendment, Was Not an "Exercise" of a General Power of Appointment.

U. S. v. Merchant's Nat'l Bank of Mobile, Exr., 261 F.2d 570 (5th Cir. 1958)

Keating v. Mayer, 136 F. Supp. 286 (E.D. Penn. 1955), aff'd 236 F.2d 478 (3rd Cir. 1956)

Butterdick v. Wright, 148 Ind. 477, 47 NE 931 (1897)

Farnum v. The Pennsylvania Company for Insurance on Lives and Granting Annuities, 87 N.J. Eq. 108, 99 Atl. 145 (1916), *aff'd* 87 N.J. Eq. 652, 101 Atl. 1053 (1917)

In the Matter of Lucy Spitzmuller, 279 App. Div. 233, 109 N.Y.S. 2d 1 (1951), *aff'd* 304 N.Y. 608, 107 NE 2d. 91 (1952)

II.

The 1945 Amendment Releasing All Rights to Amend or Terminate the Trust Was Not an "Exercise" of a General Power of Appointment, and Was Expressly Exempted from Tax Liability.

U. S. v. Hubner, 285 F.2d 29 (9th Cir. 1960), *affirming* 187 F. Supp. 659 (S.D. Cal. 1960) (acquiessed by CIR.)
Estate of Mable Wooster, 9 T.C. 742 (1947)
Section 2041, Internal Revenue Code of 1954, c.736, 68A Stat. 385.

III.

Even if Decedent's Letter of May 16, 1931, or His Amendment of January 19, 1938, or His Release of 1945, Were an Exercise of a General Power of Appointment, Such Exercise Would Not Be a Disposition of the Type Described in Sections 2041(a)(1)(B) and 2036 of the Internal Revenue Code of 1954.

Bernard E. Denzer, 29 T.C. 237 (1957)
Section 2036, Internal Revenue Code of 1951, c.736, 68A Stat. 382
Section 2041, Internal Revenue Code of 1954, c.736, 68A Stat. 385

IV.

Decedent's Letter of May 16, 1931, as Ratified by His Amendment of January 19, 1938, When Considered in the Light of the New York Statute Prohibiting Accumulations of Trust Income Except During the Minority of a Benefi-

ciary, Was Not an Exercise of a General Power of Appointment.

In re Burnham's Estate, 82 N.Y.S. 2d 844 (1948)
In re Clarkson's Will, 107 N.Y.S. 2d 289 (1951)
In re McKinney's Trust, 5 Misc. 2d 210, 159 N.Y.S. 2d 907 (1957)
Hutchinson v. *Ross*, 262 N.Y. 381, 187 N.E. 65 (1933)
Estate of Paul, 16 T.C. 743 (1951)
Albert J. Appell, 10 BTA 1225 (1928)
Commissioner v. *Morris*, 90 F. 2d 962 (2d Cir. 1937)

ARGUMENT

History of Taxation of Powers of Appointment

It may be helpful to an understanding of the case to review briefly the unique statutory history of the taxation of powers of appointment. The first revenue act which imposed an estate tax, the Revenue Act of 1916, c.463, 39 Stat. 756, failed to make any mention of the power of appointment. In 1917, the Treasury amended its regulations to provide that property passing under a general power of appointment exercised by the donee be included in the donee's estate for Federal estate tax purposes (T.D. 2466, 32 Treas. Dec. No. 15, 1917). The United States Supreme Court, recognizing the concept of property law that the appointee receives the property from the donor of the power rather than the donee, refused to approve the amended regulations in the absence of specific statutory authority. *U. S.* v *Field*, 255 U.S. 257 (1921).

Congress incorporated a specific provision regarding the exercise of a general power of appointment in the Revenue Act of 1918, c.18, 40 Stat. 1057. Section 402(e) of that act provided that the appointed property be included in the appointor's gross estate—

> "To the extent of any property passing under a general power of appointment exercised by the decedent (1) by will, or (2) by deed executed in contemplation of, or intended to take effect in possession or enjoyment at or after, his death, except in case of a bona fide sale for a fair consideration in money or money's worth . . . "

With little change, the above statute remained in effect during the next two decades and until the passage of the Revenue Act of 1942, c.619, 56 Stat. 798.

The Revenue Act of 1942 drastically changed the prior law. Many special powers as well as general powers were made taxable and the tax attached to the mere existence of the power at date of death of the donee whether or not it had been exercised.

The principle of including in the taxable estate of the donee property subject to a power to appoint, even though not exercised, was entirely new and would have subjected to estate tax many trusts not theretofore believed to be taxable. Congress recognized the inequity of having the statute apply to powers created prior to the adoption of the 1942 Revenue Act and provided for a tax-free release of a general power of appointment created prior to 1942, if such release were effected before a certain date. This grace period within which to effect a tax-free release of a general power of appointment was extended from time to time, until finally the adoption of the Powers of Appointment Act of 1951, c. 165, 65 Stat. 91 restored the law as to pre 1942 powers as it existed prior to the adoption of the Revenue Act of 1942.

As was stated in the Senate Committee Report explaining the 1951 Act:

> "Section 1 (2) of the bill amends section 811(f) of the code, relating to estate tax on powers of appoint-

ment. The new section 811(f)(1) deals with preexisting powers, i.e., powers created on or before October 21, 1942, the date of enactment of the 1942 act. As to such powers it restores the situation which existed prior to that date, i.e., only the exercise of a general power of appointment is taxed. An amendment by your committee makes it clear that a complete release of a preexisting power at any time is not taxable.

"The former statute taxed property 'passing' under a general power of appointment exercised by the decedent. This sometimes gave rise to litigation where the decedent appointed part or all of the property to persons who would also have taken it under the terms of the original instrument creating the power. The bill eliminates this possibility by taxing all property with respect to which the decedent has 'exercised' a general power of appointment.

"With this exception, the intent of the bill is to restore the law regarding preexisting powers as it existed prior to the 1942 act." (Senate Report 382, 82nd Congress; 2 U.S. Code, Congressional and Administrative Services (1951) 1530, 1532).

Section 811 (f) (1) of the Internal Revenue Code of 1939, c.2, 53 Stat. 120 (as amended by Section 2(a) Powers of Appointment Act of 1951, c.165, 65 Stat. 91), provides as follows:

"Powers of Appointment—

"(1) Property with respect to which decedent exercises a general power of appointment created on or before October 21, 1942.—To the extent of any property with respect to which a general power of appointment created on or before October 21, 1942, is exercised by the decedent (1) by will or (2) by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate

under subsection (c) or (d); but the failure to exercise such a power or the complete release of such a power shall not be deemed an exercise thereof."

The above statute was carried over almost intact into the 1954 Revenue Code and now stands as Section 2041 (a) (1) of the Interral Revenue Code of 1954, c.736, 68A Stat. 385. Thus, different rules are provided respecting powers of appointment created on or before October 21, 1942 and those created after such date. As to powers created after October 21, 1942, the mere "possession" of a general power of appointment, whether or not exercised, requires the inclusion of the appointive property in the taxable estate of the donee of the power. As to powers created prior to October 21, 1942, taxability depends upon (1) possession and (2) exercise of the power.

A consideration of the foregoing history is important because it explains the setting at the time decedent, who had been given the power by his father's trust of July 10, 1929 to amend or terminate the trust, released such power by a formal document executed on June 20, 1945. By releasing the power, the law permitted him to avoid its being taxed.

I.

NEITHER DECEDENT'S LETTER OF MAY 16, 1931 REQUESTING THE ENTIRE INCOME RATHER THAN SO MUCH AS THE TRUSTEE MIGHT DETERMINE, NOR DECEDENT'S AMENDMENT OF JANUARY 19, 1938 RATIFYING THIS ACTION, NOR HIS RELEASE ON JUNE 20, 1945 OF HIS POWER TO AMEND OR TERMINATE THE TRUST, CONSTITUTED AN EXERCISE OF A GENERAL POWER OF APPOINTMENT.

The value of the corpus of Matthew Gartland's trust should not be included in the gross estate of his son Leo

Gartland, because at no time did decedent Leo Gartland exercise a general power of appointment over his father's trust.

Decedent was not given a general power of appointment in these specific words, but petitioner concedes that the power given to him by paragraph 8 of the trust to terminate the trust was equivalent to a general power of appointment and the power to amend also could be a general power, depending upon the nature of the amendment. This power to terminate or amend having been given to him by the terms of the original trust agreement dated July 10, 1929, it was a pre 1942 power of appointment. On this the Government, petitioner and the Tax Court agree.

Decedent did three, and only three, things respecting his father's trust which the Government contends had any bearing on the question of taxability of the trust: (a) On May 16, 1931, he requested the trustee to pay him all the income of the trust rather than "so much" of the income as the trustee shall deem advisable (A-32); (b) on January 19, 1938, he formerly amended the trust to provide that all of the net income should be paid to him during his life (A-33); and (c) on June 20, 1945, he executed a formal document releasing all power to amend or terminate the trust (A-36).

Except for this change in the language dealing with the income during decedent's lifetime, and another which is not in issue, the income and principal of the trust devolved according to its terms and as originally prescribed by the settlor, Matthew Gartland, on July 10, 1929. The decedent made no change whatever in the dispositive provisions of the trust which control the distribution of corpus of the trust or any other benefits which would accrue after his death. The decedent's widow and his children received, or will receive, income and principal of the trust after decedent's death not because of any exercise of a power of

appointment by decedent or any other act, expression of will or desire by decedent, but rather by reason of decedent's father's wishes and desires as expressed in the trust instrument (A-26-7).

If decedent had taken no action respecting his father's trust other than to accept so much of the income from time to time as the trustee, in its discretion, should pay to him, the corpus of the trust clearly would not be includable in his estate for Federal estate tax purposes, because the trust was created prior to October 21, 1942 and, as previously pointed out, Section 2041 expressly provides that the mere possession without exercise of a pre 1942 general power of appointment does not give rise to the imposition of the estate tax.

If decedent had taken no action respecting his father's trust other than the execution of the document dated June 20, 1945 releasing his power to amend or terminate the trust, the property in the trust would not be taxable as a part of his estate. Section 2041 in precise words states, ". . . the complete release of such a power shall not be deemed an exercise thereof."

It is because the June 20, 1945 release was preceded by the May 16, 1931 letter requesting the income, and the ratifying amendment of 1938, that the respondent asserted, and the Lower Courts held—erroneously we maintain—that the property in the trust should be included for estate tax purposes in the gross estate of the decedent. The Court erroneously held that decedent's taking of withheld income of $547.35 and of all the income for life rather than "so much" as the trustee might give to him, so changed the beneficial interests of the other beneficiaries as to amount to an "exercise" of a pre 1942 general power of appointment over the entire $258,968.29 of trust property. The Lower Courts further erred in holding that the taking of the income followed by the 1945 tax free release was the equiv-

alent of a transfer by decedent of his own property for the benefit of the other beneficiaries of the trust and the retention by decedent of the income of the transferred property for his life, and that by reason of this transfer the entire property of the trust must be included in decedent's gross estate by virtue of Section 2041(a)(1)(B) and 2036 of the Internal Revenue Code of 1954.

The Letter of May 16, 1931, as Ratified by the 1938 Amendment, Was Not an "Exercise" of a General Power of Appointment.

With respect to the letter of May 16, 1931, as ratified by the 1938 amendment, petitioner maintains that the Tax Court erred in holding that the letter was an exercise of a pre 1942 power of appointment for two reasons.

1. Decedent's letter of May 16, 1931, as ratified by his amendment of January 19, 1938, was not an exercise of a general power of appointment because it was, in fact, a nullity. New York statutes in effect at the time of the creation of the trust and at the time of the date of the letter and ratifying amendment prohibited accumulations of income in trust except during the minority of a beneficiary. Thus, even without the letter of May 16, 1931 and the amendment of 1938, the trustee of the Matthew Gartland trust was required by New York law to distribute to decedent during his lifetime all rather than "so much" of the income as the trustee, in its discretion, might deem advisable. This proposition is dealt with in Part III of this argument.

2. The New York statutes aside, the letter of May 16, 1931, as ratified by the 1938 amendment, was not an exercise of a general power of appointment because it dealt solely with the income of the trust during decedent's life-

time and did not attempt to direct distribution after decedent's death.

The decedent, by his letter of May 16, 1931, as amended in 1938, executed an instrument which in the normal sense of the word could not be considered an "exercise" of a general power of appointment. Neither this letter nor the ratifying amendment made any change whatsoever in the dispositive provisions of his father's trust. Those named by the trust instrument as beneficiaries of the trust after decedent's death are enjoying the benefits of the trust exactly as provided by decedent's father when he executed the instrument, and these benefits are flowing to them not by reason of the beneficence of the donee, but rather by reason of the wishes of decedent's father as expressed in the trust instrument.

The word "exercise" as it relates to the taxation of appointed property first appeared in the statute in 1918, Section 402(e) Revenue Act of 1918, c.18, 40 Stat. 1057. It remained intact until eliminated by the Revenue Act of 1942, c.619, 56 Stat. 798, but was restored as to pre 1942 general powers of appointment by the Powers of Appointment Act of 1951, c.165, 65 Stat. 91. Hence, by reenacting the pre 1942 law with the requirement that a general power of appointment must be "exercised" to impute taxability to the appointed property, Congress necessarily re-adopted the word "exercise" as theretofore construed by the courts. On this specific point, in *Keating* v. *Mayer*, 136 F. Supp. 286 (E.D. Penn. 1955) at page 290, affirmed 236 F.2d 478 (3rd Cir. 1956), the court said:

> "The instant case calls for an application of the pre-1942 law, excepting therefrom only the requirement that the property pass by the exercise of that power. The decisions which had construed what was an exercise of an appointive power under the pre-1942 laws were known to Congress. Since, in situations like the

present, Congress made only the change which eliminated the requirement that the property pass. it is reasonable to infer that Congress intended no change from prior judicial determination of what constituted exercise of a power."

The cases arising under the pre 1942 statute decided that state law governs the question of whether an "exercise" of a general power of appointment by a donee has legal validity. *Helvering* v. *Grinnell*, 294 U.S. 153 (1935); *Estate of Rogers* v. *Commissioner*, 320 U.S. 410 (1943). See also *Helvering* v. *Stuart*, 317 U.S. 154 (1942). This same position has been taken respecting the word "exerise" in the statute restoring the pre 1942 law respecting powers of appointment. *U. S.* v. *Merchants National Bank of Mobile, Exr.*, 261 F.2d 570 (5th Cir. 1958), affirming 156 F. Supp. 827; *Keating* v. *Mayer*, 236 F.2d 478 (3rd Cir. 1956), affirming 136 F. Supp. 286.

Under the applicable local law, intent is a necessary element of an exercise of a general power of appointment irrespective of whether that law be that of Indiana, the domicile of the donor, New Jersey, the law selected by the donor as that by which the instrument shall be governed, or New York, the situs of the trust since August 6, 1929. *Bullerdick* v. *Wright*, 148 Ind. 477, 47 NE 981 (1897); *Farnum* v. *The Pennsylvania Company for Insurance on Lives and Granting Annuities*, 87 N.J. Eq. 108, 99 Atl. 145 (1916), *aff'd* 87 N.J. Eq. 652, 101 Atl. 1053 (1917); *In the Matter of Lucy Spitzmuller*, 279 App. Div. 233, 109 N.Y.S. 2d 1 (1951), *aff'd* 304 N.Y. 608, 107 N.E. 2d 91 (1952).

An examination of decedent's letter of May 16, 1931 requesting the income of the trust, and the ratifying amendment of 1938, reveals no express words of appointment—no words attempting to direct or control the disposition of the property upon the death of the donee. Neither in the letter of May 16, 1931, nor the ratifying amendment of

1938, did the donee recite that he was appointing the trust property to his wife and children or to anyone else. There is nothing in any of these documents which manifests any desire on his part to exercise the privilege given to him by his father to transfer or otherwise control the disposition of his property upon his, the donee's, death.

Decedent was entitled to "so much" of the income as the trustee, in its discretion, might distribute to him. Decedent was the primary beneficiary, and was the only designated income beneficiary, of the trust during his lifetime. The whole scheme of the trust demonstrates that he was the first object of the settlor's bounty. In addition, decedent had full power to amend or terminate the trust.

In the light of these facts there can be little doubt but that the trustee would have distributed to the decedent all of the income if decedent had orally expressed a mere wish and desire for it. Thus, as a practical matter and under a reasonable construction of the trust instrument decedent did not need to write the letter of May 16, 1931, nor execute the formal amendment of 1938, in order to obtain for himself all, rather than "so much", of the income of the trust. These documents evidence that there was no intention on the part of the decedent to control the disposition of the trust property after his death, although an essential condition of "exercise" is an intention to give or transfer—to control the disposition of the property after the death of the holder of the power of appointment.

The Tax Court, ignoring this evidence of lack of intent, however, held that the effect of decedent's letter of 1931, and the ratifying amendment of 1938, was to take away from the remaindermen (a) $547.35 of income which had been accumulated and (b) an unknown amount of income which but for such action might have been accumulated by the trustee in its discretion and added to principal. This is the extent of the values that the Tax Court holds were

affected by decedent's action. Thus, because of the withholding from the remaindermen of $547.35 and an uncertain amount of income which might have been accumulated, the Tax Court would subject to tax a trust having a value of approximately $258,000.00.

In support of its position that the letter of May 16, 1931, as ratified by the 1938 amendment, was an exercise, the Tax Court relies upon the *Estate of Rogers* v. *Commissioner*, 320 U.S. 410 (1943). The petitioner submits that the *Rogers* case is not controlling in the instant case because the *Rogers* case was dealing with an unchallenged exercise of a general power of appointment which contained a positive expression of will by a donee who intended to and did, in fact, exercise his power and dominion over the entire plan of distribution of a trust by providing specific instructions in the instrument by which he exercised his power, outlining a new dispositive scheme. In the original instrument, the donor gave the donee, who was the decedent, a general testamentary power of appointment over certain property with limitations over in default of the appointment to the heirs of the son who were, upon the donee's death, his widow, a daughter, and a son. The donee, in his will, unlike Leo M. Gartland, who made no attempt to specify who should take at or after his death, exercised the power and created the following interests: a fraction of the appointable property in three equal shares to the wife, daughter and grandson; of the balance, two equal shares were put in trust for the benefit of the widow and daughter, respectively, while a third equal share was appointed outright to the grandson. The donee made no appointment to his son.

In the instant case, the decedent, by his letter of May 16, 1931, as ratified by the 1938 amendment, executed an entirely different type of document (A-32, 33). This letter did not deal with the pattern of distribution of the trust at

or after decedent's death nor did it deal with corpus, but rather dealt only with decedent's income from this trust, which income was already under decedent's dominion and power. There was no substitution of his will and donative intent for that of decedent's father nor was there any attempt by decedent to direct the distribution of property at or after his death.

Thus, the *Rogers* case is clearly distinguishable and does not support the decision of the Tax Court in the instant case. Petitioner maintains, therefore, that the Tax Court erred in deciding that decedent's letter of May 16, 1931, as ratified by the 1938 amendment, was an exercise of a general power of appointment.

II.

THE 1945 AMENDMENT RELEASING ALL RIGHTS TO AMEND OR TERMINATE THE TRUST WAS NOT AN "EXERCISE" OF A GENERAL POWER OF APPOINTMENT.

The question as to whether decedent's release of June 20, 1945 in and of itself was an exercise of a pre 1942 general power of appointment is easily disposed of, as Section 2041(a)(1) expressly states that a complete release of such a power shall not be deemed to be an exercise thereof. Thus, decedent's release, when considered without reference to decedent's earlier acts, clearly falls within the statute and cannot be considered to be an exercise.

The Tax Court has held, however, that because the release was preceded some 14 years earlier by what it regarded as the exercise of a general power of appointment which shifted beneficial interests under the trust, namely, decedent's letter of May 16, 1931, and ratifying amendment, the release became an "exercise" rather than a "release." The Tax Court stated in its opinion, "To

hold otherwise would permit an effective exercise of a general power of appointment in such a manner as to dispose of the property as the holder of the power wished but at the same time permit the property subject to the power to escape the Federal estate tax because of a surrender or relinquishment of the power after it had served the holder's purposes."

The Tax Court's conclusion is completely unfounded. It would appear from a reading of Section 2041(a)(1) that if there has been a taxable exercise of a pre 1942 general power of appointment, a later release of the power will not operate to nullify the tax implications of such an exercise. Likewise, if the previous exercise were an exercise which did not require the property to be included in the gross estate of the donee for estate tax purposes, i.e., a disposition falling outside the scope of Sections 2035-8, a subsequent release would add nothing and the prior exercise would remain non-taxable.

If the decedent's letter of May 16, 1931, as ratified by the 1938 amendment, was not an exercise by a disposition which required the appointed property to be included in the donee's taxable estate, it is immaterial whether it was followed by a release or not, and a subsequent release should not cause taxability. For example, if decedent withdrew one-half of the corpus and gave it away completely during his lifetime without retaining any string whatever, such withdrawn portion of the corpus would not be included in his estate whether he later released his power to amend or terminate the trust or not. The power could be exercised from time to time by partial and successive exercises and the question of taxability arises only as to that part of the property which was appointed and not to the balance. *Estate of Mable Wooster*, 9 T.C. 742 (1947).

If Congress had meant to have a release of a pre 1942 general power of appointment operate as an "exercise," it would have so stated. The language of Section 2041 of the 1954 Internal Revenue Code is clear and unambiguous. It provides that ". . . the failure to exercise such a power or the complete release of such a power shall not be deemed an exercise thereof."

In *U. S.* v. *Hubner*, 285 F.2d 29 (9th Cir. 1960), *affirming* 187 F. Supp. 659 (S.D. Cal. 1960), it was expressly held that a "release" of a pre 1942 general power of appointment did not constitute an "exercise" thereof. In that case the powers released by the decedent, Gertrude R. Hurst, were granted to her by (a) a trust created by her husband on October 13, 1942 and (b) an insurance contract providing for the retention by the insurer of the proceeds of a policy which matured in 1929. Decedent had the right to withdraw the proceeds of the insurance policy and to revoke the trust agreement. The Government contended (1) that since the powers given to Gertrude R. Hurst were revocable at any time by her husband prior to his death on March 6, 1946, they were not pre October 21, 1942 powers and (2) that the releases by Gertrude R. Hurst on June 25, 1947 of her right to withdraw the insurance proceeds and her right to revoke the trust constituted an "exercise" of her general powers of appointment. The Court of Appeals affirmed the holding of the District Court that the decedent's powers were pre October 21, 1942 powers and that the "releases" did not constitute an exercise of a general power of appointment. As to the latter, the Court stated—

> "The fact that the wife released her rights to withdraw the insurance funds and revoked the trust on June 25, 1947 was not an exercise of such powers by the express language of Section 2041(a)(1)(B)."

In view of the *Hubner* case and the clear language of Section 2041, petitioner maintains that Leo Gartland's 1945 amendment "releasing" his power to amend or terminate the trust was not an "exercise" of a pre 1942 general power of appointment under Section 2041 of the Internal Revenue Code of 1954.

III.

EVEN IF DECEDENT'S LETTER OF MAY 16, 1931, OR HIS AMENDMENT OF JANUARY 19, 1938, OR HIS RELEASE OF 1945, WERE AN EXERCISE OF A GENERAL POWER OF APPOINTMENT, SUCH EXERCISE WOULD NOT BE A DISPOSITION OF THE TYPE DESCRIBED IN SECTIONS 2041(a)(1)(B) AND 2036 OF THE INTERNAL REVENUE CODE OF 1954.

It is petitioner's contention that even if decedent's letter of May 16, 1931, or his 1938 amendment, or his 1945 release, or any combination of them, were considered to be an exercise of a pre 1942 general power of appointment, such an exercise would not be one which subjects the Gartland trust property to the Federal estate tax, because such exercise would not have been by a disposition of the type described in Section 2041(a)(1)(B), c.736, 68A Stat. 385.

The type of disposition which will invoke the estate tax by reason of the exercise of a general power of appointment is carefully defined by Section 2041(a)(1)(B) as an exercise by the decedent—

> "(B) by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includable in the decedent's gross estate under sections 2035 to 2038, inclusive: . . ."

The Government contends, and the Tax Court has held, that Section 2036, c.736, 68A Stat. 382, is applicable to the facts in the instant case. This section as it pertains to this case provides in part that—

> "The value of the gross estate shall include the value of all property . . . to the extent of any interest therein of which the decedent has at any time made a transfer, . . . by trust or otherwise, under which he has retained for his life . . . (1) the possession or enjoyment of, or the right to the income from, the property . . .".

It is petitioner's position that even if the May 16, 1931 letter, the 1938 amendment, or the 1945 release, had been an exercise of a pre 1942 general power of appointment, such exercise would not have been by a disposition which transferred the trust property and retained to decedent a life estate and, therefore, such disposition would not fall within the scope of Section 2036 and would not have been a disposition within the definition contained in Section 2041(a)(1)(B). It is true that the trust agreement in the instant case contains provisions transferring property of the trust to beneficiaries other than decedent at the time of decedent's death, and there is a provision directing the trustee to distribute so much of the income of the trust as it might determine to decedent during his lifetime (A-26-7). Both of these provisions of the trust, however, were contained in the original trust agreement creating the trust, which agreement was executed by decedent's father, and at no time did decedent change the provisions providing for the distribution of trust property at his death, alter the period of time during which benefits should be paid him, nor did he adopt such provisions as his own in a new transfer of the property to the trust.

Even by assuming an "exercise" and resolving all doubts in favor of respondent, the most that decedent can be said to have transferred to or retained for himself was $547.35 of income which had been previously withheld from him by the trustee plus that uncertain and indeterminable amount of income which the trustee, in the absence of the decedent's letter of May 20, 1931, as ratified by his amendment in 1938, (ignoring the New York law prohibiting accumulations of income), might have accumulated and added to principal during decedent's lifetime. Even with these assumptions, there was clearly no transaction which met the requirements of Section 2036.

The Tax Court's decision that decedent by requesting the income made a transfer of the trust property and also retained for his life the right to income is the equivalent of saying that decedent terminated the trust and created a new trust on the same terms except that he retained for his life the right to all rather than "so much" of the income. Such a decision is unreal and, in reality, creates a fiction which has no basis in law or in fact. As was stated in *Bernard E. Denzer*, 29 T.C. 237 (1957), at page 243:

> "We do not think that the decedent, by creating these vested interests through the exercise of his power to modify, can be said to have made transfers of anything, since the beneficiaries named under this power to modify were the very same beneficiaries who would have taken in the event this power were never exercised by decedent. See Rogers' Estate v. Helvering, 320 U.S. 153; Edith Evelyn Clark, 47 B.T.A. 865. But even if we assume that a transfer were made, it could hardly be argued that a life interest was reserved by the decedent in connection with such transfer. Decedent's life interest in a remaining half of the trust was unchanged. The agreements of 1940 did not touch this but merely left it intact as it existed under the terms of the trust set up by the original settlor. To say that

> the decedent made a transfer here by naming these beneficiaries, through the exercise of his donated power to modify, and then reserved a life interest in himself in conjunction with such transfer, is to create a fiction."

Thus, the actions of decedent during his lifetime, consisting of his letter of May 16, 1931, his 1938 amendment, and his 1945 release, did not constitute the exercise of a pre 1942 general power of appointment by a disposition of the type upon which Congress has chosen to impose the estate tax, as none of these events can be said to have transferred the property of the trust by a disposition which retained to decedent the income from the property during his lifetime, and none were, therefore, an exercise by a disposition of the type described in Section 2041(a)(1)(B).

IV.

DECEDENT'S LETTER OF MAY 16, 1931, AS RATIFIED BY HIS AMENDMENT OF JANUARY 19, 1938, WHEN CONSIDERED IN THE LIGHT OF THE NEW YORK STATUTE PROHIBITING ACCUMULATIONS OF TRUST INCOME EXCEPT DURING THE MINORITY OF A BENEFICIARY, WAS NOT AN EXERCISE OF A GENERAL POWER OF APPOINTMENT.

Petitioner maintains under Part III of this brief that neither decedent's letter of May 16, 1931 requesting all rather than "so much" of the income, nor his amendment to the trust of January 19, 1938 ratifying his letter of May 16, 1931, could have been or were an exercise of a general power of appointment. Neither the letter nor the amendment transferred any property in the trust or altered any beneficial interest under the trust because the trustee was required by New York law to do the very thing that the

letter and formal amendment requested it to do, that is, pay all, rather than "so much," of the income to the decedent. Thus, the letter and amendment were both nullities having no economic or legal significance as all of the income would be payable to decedent whether the letter and amendment had been executed or not.

Matthew F. Gartland, settlor of the trust in this case, was a resident of Marion, Indiana, as was his son, Leo, the primary beneficiary (A-22). The trust provided that it was the duty of the trustee "to pay over to my son, Leo M. Gartland, so much of the income as the trustee in his discretion shall deem advisable and to accumulate the remaining income and add it to the principal of the trust fund during the life of my said son" (A-26).

When this trust was created in 1929, an Indiana statute forbade any accumulation of income from personal property in any trust except during the minority of the income beneficiary. Burns Indiana Stats. Ann., 1933, § 51-102. This statute was in force for 92 years, from 1853, when it was adopted, until 1945, when it was repealed. Burns Indiana Stats. Ann. 1951, § 51-102.

During this same period, New York had similar statutes which prevented accumulations of income from both real and personal property. These statutes required that all income directed *or permitted* to be accumulated must instead be paid our currently to the income beneficiary who would take in the absence of the invalid provision. N. Y. Real Property Law, § 61, repealed N. Y. Sess. Laws 1959, c. 454 §§ 1, 4; N. Y. Pers. Prop. Law, § 16, repealed, N. Y. Sess. Laws 1959, c. 453 §§ 1, 4. The New York courts have squarely held that a trust provision giving the trustee discretion to distribute or accumulate income violates the statute; that the statutes strike down the provision which would permit accumulation; and that the entire income must be distributed to the income beneficiary. *In re Burn-*

Ham's Estate, 82 N.Y.S. 2d 844 (1948). Presumably, the same result would have been reached by the Indiana courts applying a substantially identical statute although there are apparently no Indiana decisions on the point. Thus, under the law of the situs of the trust, New York, and that of the creator's domicile, Indiana, the direction to accumulate income in this trust during decedent's lifetime was void, and if either law was applicable to the Gartland trust, decedent legally would have been entitled to all of the income during his lifetime regardless of whether he so amended the trust.

The Gartland trust named S. Roswell Shepard, an individual who was a resident of New Jersey, as the original trustee (A-26). Shepard acknowledged receipt of delivery of the trust instrument in New Jersey and the trust instrument itself provided that it should be controlled by the laws of the State of New Jersey (A-30, 31). Other circumstances and developments, however, would indicate that it was the intention of the parties at the time of the creation of the instrument that the situs of the trust would be New York and that S. Roswell Shepard was merely a conduit between Matthew Gartland and The National City Bank of New York, which was to be the permanent trustee. The trust agreement, as executed, provided that The National City Bank of New York could be appointed corporate co-trustee with Shepard, and that the Farmers Loan and Trust Company of New York could be substituted as successor trustee (A-29). The chain of events which occurred, commencing with the execution of the instrument, established beyond peradventure that New York, not New Jersey, was the intended situs of the trust as follows:

1. The trust was executed by Matthew Gartland on July 10, 1929. Eight days later, on July 18, 1929, S. Roswell Shepard acknowledged delivery of the agreement in New Jersey. Five days later, on July 23, 1929, Shepard appointed The National City Bank of New

York as co-trustee and Farmers Loan and Trust Company of New York as successor co-trustee (A-22).

2. Fourteen days later, on August 6, 1929, The National City Bank of New York accepted its appointment and Shepard resigned. Shepard had been sole trustee for just five days and had been co-trustee thereafter for just fourteen days (A-22).

Within three weeks after the date of the acceptance of the trust, the New York corporate trustee, which had been named in the original instrument, was sole trustee and thereafter, to the present time, the sole trustee has been a corporate trustee located in the State of New York. Thus, the only points of contact with the New Jersey jurisdiction which have occurred during the entire term of the trust, which to the present date has extended more than thirty-one years, were (a) the acceptance of the trust in New Jersey, (b) the residence in New Jersey of S. Roswell Shepard, who was the initial trustee for the first five days and was a co-trustee for the next fourteen days of the trust, and (c) the provision in the trust instrument that the laws of the State of New Jersey would apply to the trust.

Under these circumstances, even if the situs of the trust had been the State of New Jersey for a few days or possibly weeks in the summer of 1929, the situs was permanently shifted to the state of New York when The National City Bank of New York became sole trustee and, therefore the trust was subject to the conflict of laws rules under the laws of New York as they applied to trusts having a situs in New York. Petitioner maintains that the New York conflict of laws rules require that trusts having a situs in New York can not violate New York's public policy against accumulation of income in trusts except during the minority of a beneficiary and that the trustee of the Gartland trust, by reason of such public policy, was required to pay all of the income to decedent during his lifetime. This the trustee was

required to do without any demand by decedent and without any amendment of the trust.

It has been held that a testamentary trust created by the will of a non-resident decedent, but which trust had a situs in New York, could not accumulate income in the trust except during the period of minority of a beneficiary. *In re Clarkson's Will* 107 N.Y.S. 2d 289 (1951). In this case, Mrs. Clarkson died a resident of California leaving a will containing a testamentary trust which directed the trustee to pay a certain portion of the income to her son, and to accumulate the balance to be distributed to him when he attained the age of forty five. The California court ordered the transfer of the property to trustees which had been appointed in New York and the New York court in its opinion stated:

> "However, since the deceased at the time of her death was a resident of the State of California, the second question presented is whether this Court should follow the law of California, the domicile of the testatrix, or the law of New York State.
>
> [3] It is conceded that the provision of the will providing for the accumulation of income beyond the minority of the beneficiary is valid under the laws of California. Reiss v. Reiss, 45 Cal. App. 2d 740, 114 P.2d 718; In re Hardy, 62 Cal. App. 2d 958, 145 P.2d 910.
>
> On the other hand such provision for accumulation beyond the minority of the beneficiary is void under the laws of New York.
>
> [4] Since the petitioning trustees have been appointed by this Court and are administering the trust within this jurisdiction, by virtue of a decree of the California Court ordering a transfer to such trustees, this Court believes the law of this state to be controlling. [5,6] This Court is not bound by comity to effectuate a foreign law which would contravene the positive

> policy of the law of the forum and when one person sends property into another jurisdiction he subjects it to the laws of the foreign forum. Walworth v. Harris, 129 U.S. 355, 9 S. Ct. 340, 32 L. Ed. 712; Green v. VanBuskirk, 5 Wall. 307, 72 U.S. 307, 18 L. Ed. 599. Similarly the New York Courts have held that comity does not require them to substitute the policy and laws of a foreign state in place of its own. Clough v. Gardiner, 111 Misc. 244, 182 N.Y.S. 803; Pennington v. Townsend, 7 Wend. 276."

The New York courts have held in other cases that the laws of New York will apply to trusts created by residents of other states when the situs of the trust is located in New York and the trustee is also a resident of New York. *In re McKinney's Trust,* 159 N.Y.S. 2d 907 (1957); *Hutchison* v. *Ross,* 262 N. Y. 381 (1933).

The settlor of a trust is usually privileged to specify by what law his instrument is to be construed but such an agreement or specification is subject to the public policy of the jurisdiction by which the agreement would otherwise be governed. *In re Clarkson's Will,* 107 N.Y.S. 2d 289 (1951); *In re McKinney's Trust,* 159 N.Y.S. 2d 907 (1957); *Hutchison* v. *Ross,* 262 N. Y. 381 (1933); *Rabel, The Conflict of Laws; A Comparative Study*, Vol. 2, 583.

Thus, as in the *Clarkson* case, the provision in the trust in the instant case specifying that the law of New Jersey shall apply to the trust would not be sufficient to override the declared public policy of the law of New York, which was the situs of the trust, and the trustee would have been required to distribute to decedent all of the income of the trust regardless of whether decedent had completed the May 16, 1931 letter or the ratifying amendment of 1938. Under these circumstances, decedent's letter of May 16, 1931 requiring the trustee to do something he already was required to do therefore had no effect whatsoever upon the rights

and beneficial interests under the trust, was a useless act and a nullity, and was not, in law or fact, the exercise of a pre 1942 general power of appointment. *Estate of Paul*, 16 T.C. 743 (1951).

It may be helpful to point out that immediately prior to the creation of the trust by Matthew Gartland, the Board of Tax Appeals held in *Albert J. Appell*, 10 BTA 1225 (1928), that income which had previously been accumulated by a trustee pursuant to an invalid accumulation provision in a trust subject to the laws of the State of New York was to be taxed to the beneficiaries who were entitled to it, not to the trustee even though such income had not actually been distributed until a later year. In a later case, *Commissioner* v. *Morris*, 90 F. 2d 962 (2d Cir. 1937), the second circuit arrived at the same result.

Thus, the Federal courts have not hesitated to recognize the tax implications of the New York laws prohibiting accumulations and have applied such laws in determining the impact of the Federal income tax, and such laws should also be given effect in determining the question of whether decedent's letter of May 16, 1931, as ratified by his amendment of 1938, was an exercise of a pre 1942 general power of appointment. The decedent's letter merely directed that that be done which the law of New York would require to be done in the absence of the letter. Petitioner submits, therefore, that if the substance of the letter is to be considered, the letter can not be considered the exercise of a pre 1942 general power of appointment.

The decision of the Court of Appeals is in conflict with decisions of other Courts of Appeal and with some prior decisions of this Court.

In a Petition for Rehearing, we undertook to point out some of the errors committed by the Court in its Opinion, and we repeat them herein.

I.

It is respectfully suggested that the Lower Court has misapprehended the New York law as to who is entitled to the income of a discretionary trust, when the direction to accumulate income is invalid. The Court, on page 12 of its opinion, assuming an invalid direction to accumulate, states that the accumulated income would have been paid over to the person or persons presumptively entitled to the next eventual estate. When the accumulation is invalid and there is no disposition of such accumulation in the instrument, the rule stated by the Court would apply. It is in this category that the cases cited by the Court on page 12 of the opinion are valid precedents. In all of these cases the New York Courts found there was no indication of a valid disposition in the instrument of the invalidly accumulated income and that such income must go over to the person or persons presumptively entitled to the next eventual estate.

However, if, as in the instant case, the trustee has discretion to pay or not to pay the income beneficiary with no numerical monetary limits set upon the amount so payable, the New York courts will strike the invalid direction to accumulate and give the full income to the present income beneficiary. This is done because the courts consider the trustees' full discretion as being a valid disposition to the income beneficiary: only the direction to accumulate is void. *In re Hoyt*, 101 N.Y.S. 557, 560, 116 App. Div. 217, affirmed 189 N. Y. 511, 81 N.E. 1166 (1906); *In re Baekeland's Trust*, 203 N.Y.S. 2d 724, 727 (1960); *Barbour* v. *De Forest*, 95 N.Y. 13 (1884).

The 1933 trust agreement involved in *In re Baekeland's Trust*, 203 N.Y.S. 2d 724 (1960), provided that:

> "The income from the remaining one-half of the trust estate or *so much thereof as the trustees may deem proper*, shall be paid to the grantor's daughter, Nina Baekeland Roll . . . Should the trustees pay to said Nina Baekeland Roll less than the full net income . . . any such portion . . . shall be added to the principal . . . which is to vest in the issue of Nina Baekeland Roll . . .". (Italics supplied.)

Applying Section 16 of the Personal Property Law, unaffected by the 1959 amendments, the court held the accumulation invalid and added: p. 727

> "The unlawful direction for accumulation may be stricken without thwarting the grantor's underlying purpose. There remains the valid disposition of the income in favor of his daughter, the income beneficiary, which may be given effect by ruling that the entire income is payable to her . . .".

It is difficult to read the Gartland trust agreement and find any intention of the donor that the wife or children of the deceased donee were entitled to any income or principal during the lifetime of Leo M. Gartland. The clear intention was to provide income to him and, while discretionary power was vested in the trustee, general power of amendment or termination existed in the decedent, Leo M. Gartland.

II.

Petitioner respectfully suggests that the Court in holding at page 13 of its opinion that ". . . by the taking of the life estate in the corpus of the trust, a decedent makes a disposition of such a nature whereby he transfers the property by trust or otherwise, retaining a life income," has given to Sections 2041(a)(1)(B) and 2036(a)(1) an interpretation beyond the normal meaning of the words of the statutes and beyond the intention of Congress.

(a) Section 2041(a)(1) states:

> "To the extent of any property . . ."

If decedent only took the income, then that was the extent of the exercise of his general power of appointment. The Court in effect holds that the language "to the extent" means nothing and that if only income is taken, the corpus is taxable—that eating the fruit from the tree is the same as chopping down the tree.

(b) Section 2041(a)(2) and (b) states:

". . . by a disposition . . ."

Although the tax is imposed upon the "exercise", such exercise must be "by a disposition". If decedent only took the income, then there has hardly been a "disposition". Webster's New International Dictionary, Second Edition, defines disposition as "the getting rid, or making over, of anything; relinquishment."

The Court's decision that the taking of the income was a "disposition" of the corpus fails to give to the word "disposition" its normal meaning. It is respectfully suggested that "taking" is not the same as "getting rid of".

If decedent had appointed the remainder, it would have been an exercise by a "disposition" and a retention of the income therefrom for life would have made such disposition the equivalent of a transfer under Section 2036. The appointment of the remainder is, we urge, a *sine qua non* of taxability. Whether the remainder passes under the appointment is immaterial.

(c) Assuming that *Lee* v. *Commissioner of Internal Revenue*, C.A.D.C., 57 F. 2d 399 (1932), and *Wear* v. *Commissioner of Internal Revenue*, 3rd Cir., 65 F. 2d 665 (1933), would not have been overruled if the present wording of the statute had been in effect, as the Court suggests, and assuming that these cases represent good law today, we beg leave to question their applicability to the instant case. Both of these cases involved the exercise of a general power

of appointment by will, rather than an exercise by an inter vivos disposition. Hence, both cases bear on the present Section 2041(a)(1)(A) rather than Section 2041(a)(1)(B) involved in the instant case. Moreover, in each of these cases there was an express appointment of the corpus of the appointive property.

In *Wear* v. *Commissioner of Internal Revenue*, 3rd Cir., 65 F. 2d 665 (1933), the Court, in holding that taxability does not depend upon the passing of title, speaks of the possibility of the defeasance of the estate of the remaindermen until the death of the donee of the power and states that it was only when the donee died that this risk disappeared and the interests of the remaindermen became fully vested. In evaluating this language, however, it must be borne in mind that the exercise of the power of appointment by the donee by his will could not become effective, by its very nature, until the death of the donee decedent. At any time until his death, the decedent could have changed his will and either exercised, or refrained from exercising, his power of appointment. Not death alone, but death coupled with an exercise, was the important event, as stated by the Court at page 667:

> "Death, *with an exercise of the power in their favor*, was the event that wrought the change." (Italics supplied)

Granted that an "actual transfer" is not a requirement of taxability under Section 2041(a)(1)(A), nevertheless death alone cannot impute taxability, even if death of the donee of the power causes the estate of the remaindermen to be non-defeasible. For example, a power to appoint by will is extinguished by death, thus cutting off the right of the donee to divest the remaindermen of their interests. Yet, as to a pre 1942 power, the death of the donee does

not impute taxability unless the power has been exercised. (Section 2041(a)(1)(A))

As to a pre 1942 power to appoint by inter vivos disposition (Section 2041(a)(1)(B)), such as in the instant case, death, although eliminating the possibility of defeasance of the estates of the remaindermen, does not cause the tax to attach. There must be an exercise, and by a particular method. (Sec. 2041(a)(1)(B)) Likewise, the release prior to death of the donee of a pre 1942 power, although causing the estate of the remainder interests to become completely vested, does not result in the imposition of the tax, because Section 2041 expressly says that the release of such a power shall not be deemed an exercise thereof.

Taxability in the instant case is governed by Section 2041(a)(1)(B) and depends upon (1) an exercise, (2) by a disposition, (3) of such nature that if it were a transfer of property owned by the decedent, it would be includable in the decedent's estate under Section 2036.

(d) Even the Treasury Estate Tax Regulation, 1954 Code, 25 C.F.R 20.2041-2(c) 1961, quoted at page 12 of the Court's opinion, has not interpreted the statutes as broadly as does the Court's opinion. The example from the Regulation quoted in the Court's opinion at page 14 contemplates not only an appointment of the life income to the donee of the power, but an *appointment* by the donee *of the remainder*. The example quoted by the Court at page 14 specifically recites ". . . B exercised the power in 1955 by directing that after A's death the income be paid to himself for life *with remainder to C*." (Italics supplied)

It should also be pointed out that the above example from the Regulation deals with a factual situation entirely different than the one in the instant case. In the above example, a second life estate is created and the possession and enjoyment of the remainder interest is thus postponed. In the instant case, the original trust agreement provided

a complete dispositive scheme upon the death of Leo Gartland and his taking of the income did not postpone the enjoyment of the remainder interest by the remaindermen.

(e) This Court holds, at page 13, that the effect of Leo Gartland's taking of the life estate was that he ". . . vested in or transferred, by trust or otherwise, the corpus of the trust to the remaindermen . . .".

The Court reaches this conclusion by ". . . considering that he was the owner of the corpus of the trust . . .". While the possessor of a general power of appointment is, with respect to the disposition of the property, in a position not unlike the owner, nevertheless as to pre 1942 powers, the appointive property is includable in the donee's taxable estate only to the extent that he exercises his power. Hence, the donee should not be considered as the owner of the property or any part thereof, unless he appoints such property or some part thereof.

The Court, at page 13 of its opinion, states that Section 2041(a)(1)(B) refers to a transfer of property ". . . as if it were owned by the decedent." It is respectfully pointed out, however, that it is only the property disposed of by the exercise of a power which may be so regarded. The words "if it were a transfer of property owned by the decedent" contained in Section 2041(a)(1)(B) seem to be clearly limited by the words "by a disposition." Section 2041(a)(1)(B) reads:

> "(B) by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate under sections 2035 to 2038, inclusive; . . ."

Since the decedent took only the income, it would not seem proper to assume that he was the owner of the corpus

and *a fortiori* he should not be deemed to have made a disposition of the corpus—which in fact he never did.

(1) The Courts of Appeal in the 5th, 8th and 9th Circuits have repulsed efforts of the Internal Revenue Service to construe Section 2041 in such a manner as to extend the law beyond its pre 1942 meaning. *U. S.* v. *Merchants National Bank of Mobile*, 5 Cir., 261 F. 2d 570; *U. S.* v. *Hubner*, 9 Cir., 285 F. 2d 29; *U. S.* v. *Turner*, 8 Cir., 287 F. 2d 821. In each of these cases the power of appointment had been created prior to 1942, but was revocable by the donor. The donor's death having occurred subsequent to 1942, the question was whether the general power of appointment was created prior to 1942 or subsequent thereto. In each case the Court held the power of appointment to have been created prior to October 21, 1942. In *U. S.* v. *Turner*, 287 F. 2d 827, the Court stated at page 827:

> "The contrary argument based upon the proposition that the 'creation' of a power should be coincident with valid includability of the appointive property in the holder's gross estate is not unattractive. This gives creation a pragmatic interpretation. We feel, however, that too much time has elapsed and too many cases have been decided for us now to establish a standard of this kind. This approach, also, might well penalize the unwary and be contrary to the policy behind the 1951 legislation."

The Court of Appeals distinguishes *Helvering* v. *Grinnell*, 1934, 294 U.S., 153, claiming that the Statute considered in that case had the words, "property passing", and that the present act does not contain those words. In the instant case, the decedent, by the exercise of his power, could take any part of the income, all of the income, any part of the corpus, or all of the corpus. He took the

income, but did not touch the corpus of the Estate. He *released* his power of appointment which, in effect, was a *renunciation* of his right to take the corpus of the Estate. For nearly thirty (30) years, the Federal Courts have uniformly and consistently followed *Brown* v. *Routzahn*, 63 F. 2d, 914 (1933), Certiorari Denied, 290 U.S., 641, wherein the Court held that the renunciation by a devisee of a legacy was permissible, and that the same was not includible in his Estate, or subject to Gift Tax:

> "The decedent never owned or had control of the property as donee. All that he had was a right to accept. Coupled with this right was an equal right to reject. . . . He did reject . . . what it (Treasury Department) did was to collect a tax, not upon the transfer of an interest in property, but upon the exercise of a right to refuse a gift of property. This, we think, it had no right to do."

To the same effect was the holding by the Court of Appeals, Third Circuit, in *Higgs' Estate* v. *C. I. R.*, 184 F. 2d 427 at Page 431:

> "We do not think it realistic to find that the decedent reserved to himself under the instrument of transfer (the exercised option), an interest for his lifetime in the "property" transferred to his wife, just because he did not (and perhaps could not), transfer his whole interest to her by depriving himself of any annuity whatsoever. The annuity which the decedent had was the inevitable result, not of the incidental exercise of the option, but of the contract which was arranged by and between his employer and the insurance company pursuant to which he was entitled to an annuity in any event."

So it is in the instant case, the Trust was created by the decedent's father and the designated Trustee and was not

created by the decedent. He was the donee, and not the donor of the Trust.

In the instant case, the decedent released his right to the corpus of the Estate. The lower Courts have said that the release of a right was the same as the granting of a right to the one next in succession. This, we believe, is contrary to the Statute and prior decisions.

In *Helvering* v. *Hallock*, 309 U.S., 106, this Court held that the value of trust properties is properly included in the settlor's gross estate where the Trust Agreement expressly provides that the corpus should revert to the settlor in the event he outlives the beneficiaries. In *Spiegel* v. *Commissioner of Internal Revenue*, 335 U.S., 701, the Court held that where a trust instrument provided that during the settlor's life the trust income was to be paid to his three (3) children, and if the children died before the settlor, no provision was made for distribution of the corpus and its accumulated income, should the settlor survive all of his children, that such Trust is includible in the settlor's Estate. This case does not involve a *settlor*, but a *beneficiary* with power to take. The Court of Appeals has held that, under the language of the Trust Agreement, the beneficiary (deceased) had no rights to income under the Trust because it was solely within the discretion of the Trustee. It then contradicts itself in holding that having asked for the *income*, that constituted a taking of the income and the *corpus*, and the provision that the corpus be transferred to the alternate beneficiaries under the Trust. It made of the beneficiary a settlor creating a Trust. This holding is directly contrary to the language and spirit of this Court's Decisions.

The Decision of the Court of Appeals is in conflict with an earlier Decision by the same Court in *Kohl* v. *United States*, 226 F. 2d. 381. In this case, the Court stated:

"An estate may not be constitutionally taxed for something which, at death, was not property of decedent."

"Taxing Statutes cannot be extended by implication beyond the clear import of the language used."

"Only where gift is not complete until assignor's death can property transferred be properly included in decedent's estate for Federal Estate Tax purposes. 26 U.S.C.A., Section 811(g), Revenue Act 1942, Section 404, 26 U.S.C.A., Section 811 note."

The application of these rules to the instant case would immediately raise the question, what gift made by the decedent is incomplete until his death? When the decedent released or renounced his right to exercise dominion over the Trust of which he was the beneficiary, did he then make a gift? Was not the gift made when the Trust was created by the decedent's father in 1929? Is not the construction placed by the Court of Appeals on Sections 2036 and 2041 of the Internal Revenue Code of 1954 an extension by implication beyond the clear import of the language used?

The Decision in the instant case, for the first time in 30 years, places a construction on the Joint Resolution of Congress adopted March 3, 1931 (46 Statutes, 1516), which provided that certain transfers in contemplation of death in which the decedent retained the income interest for life were to be included in the decedent's gross estate for Estate Tax purposes in a manner so as to impose the tax *not on the donor, but on the donee*. For 30 years, the Commissioner of Internal Revenue in the administration of Estates has never made this contention. In the argument before the Court of Appeals, the Government conceded that there had been no prior case, and that this is one of first impression. The importance of this Decision cannot then be too greatly stressed. Many Trusts created over the years are

still in effect. This presents a new approach of taxation not under the clear language of the Statute, but by implication. This Court ought to speak on the subject.

RELIEF SOUGHT

Wherefore, it is respectfully submitted that this Petition for a Writ of Certiorari to review the Judgment of the Court of Appeals for the Seventh Circuit should be granted.

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APPENDIX

DECISION OF THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT
(August 4, 1961)

Before HASTINGS, Chief Judge, CASTLE, Circuit Judge, and PLATT, District Judge.

PLATT, District Judge. This is a petition by Matthew Gartland, executor of the estate of Leo M. Gartland, deceased, to review a decision of the Tax Court (34 T.C. 89, 1960) adjudging a deficiency in the Federal estate tax of $84,321.08 in his father's estate, by the inclusion of the property valued at $258,968.29 in a trust created by Matthew F. Gartland, the petitioner's grandfather.

The facts of the case are uncontroverted. On July 10, 1929, decedent's father, Matthew F. Gartland, a resident of Indiana, set up a trust whereby he transferred certain assets to S. Roswell Shepherd of West Orange, New Jersey, as Trustee. On July 18, 1929, Shepherd accepted the trusteeship and five (5) days thereafter, under the authority of the trust agreement, appointed the National City Bank of New York as co-trustee and the Farmers Loan and Trust Company as successor trustee, should the appointed co-trustee resign. The National City Bank accepted this appointment, and on August 6, 1929, Shepherd resigned as co-trustee. On January 20, 1930, the National City Bank resigned as trustee and the City Bank Farmers Trust Company, successor to the Farmers Loan and Trust Company, accepted appointment as successor trustee. At the time of Leo M. Gartland's death, on April 1, 1955, the City Bank Farmers Trust Company was still acting as trustee.

Pertinent portions of the trust created by Matthew F. Gartland provided:

> "1. In disposing of the income and principal of this trust the Trustee's duties shall be:
>
> A. To pay over to my son, Leo M. Gartland, so much of the income as the trustee in his discretion shall deem advisable and to accumulate the remaining income and add it to the principal of the trust fund during the life of my said son.
>
> B. Upon the death of my said son to pay over the income to my daughter-in-law, Irene S. Gartland, during her life.
>
> C. Upon the death of the survivor of my said son and my said daughter-in-law, to divide the principal of the trust fund into so many equal shares that there shall be one for each child of my said son then living and one for the descendants then living of each deceased child of my said son, and to dispose of the income and principal of such shares as follows:
>
> • • •"

The trust further provided that the income be paid to each child until such child attained a certain age at which time the principal was to be distributed to such child, or as each might appoint by will, and if no appointment was made to the descendants of such child, and in default of descendants the trust was to be distributed to the descendants, if any, of the son of the Settlor, and in default of descendants of the son to the descendants of the Settlor, all in equal shares *per stirpes*. (The trust was modified to avoid a violation of the rule against perpetuities. This modification is immaterial here.) The trustee in his discretion could pay the minor children, or on their behalf, such portion of the principal he deemed advisable for their use and benefit; the trustee had full power to use the trust property in any way he deemed advisable; during the life

of Leo M. Gartland, the decedent, the trustee was required to secure written approval of the decedent prior to the purchase or sale of any security which the trustee proposed to make. The trust then created a general power of appointment:

> "8. I hereby authorize and empower my son, Leo M. Gartland, during his life, to amend or terminate this agreement in whole or in part and to change any beneficial interest hereunder by delivering to the Trustee an instrument in writing executed by him. In the event of the termination of this trust by my said son, the Trustee shall pay over the principal of the trust fund to him or to such person or persons as he may designate in writing to the Trustee."

The trust also provided:

> "12. The trust hereby created shall be irrevocable, shall take effect upon acceptance by the Trustee, and in all respects shall be governed by the laws of the state of New Jersey."

On May 16, 1931, the decedent sent a letter to the trustee which read in part:

> "Owing to present conditions the writer finds it necessary to use the income of his trust. You may use this as your authority to transfer the cash in my principal account to the income account and send check at your convenience."

Pursuant to this letter, the trustee on May 19, 1931, paid the decedent $1,292.98, which was made up of $547.35 of prior accumulated income and $745.63 representing current income. The trustee in its letter replied in part:

> "We are noting on our records that you wish all of the income remitted to you."

Decedent on January 19, 1938 ratified the 1931 payment by a document addressed to the trustee. A portion thereof read:

"WHEREAS, Subdivision 'A' of Article 1 of the aforesaid trust reads as follows:

"A. . . .

"WHEREAS, Article 8 of the aforesaid trust reads as follows:

"8. . . .

"WHEREAS, by letter dated May 16, 1931 the said Leo M. Gartland partially revoked the trust by withdrawing therefrom the sum of $547.35, being income which had been accumulated prior to May 16, 1931 and added to the principal of the trust fund, and the said Leo M. Gartland, pursuant to said letter dated May 16, 1931, amended said trust to provide that the income therefrom should be paid to him until further notice, and

"WHEREAS, the said Leo M. Gartland desires to ratify, confirm and approve the said withdrawal of the said sum and said amendment made by him to said trust by said letter dated May 16, 1931.

"NOW, THEREFORE, the said Leo M. Gartland does hereby ratify, confirm and approve the withdrawal by him of the said sum of $547.35, payment of which was made to him on May 19, 1931, . . . and the said Leo M. Gartland does hereby amend said trust by striking out, canceling and annuling Subdivision 'A' of Article 1 thereof and by substituting in lieu thereof a new Subdivision 'A' of Article 1 which shall read as follows:

'A. To pay over the net income thereof to my son, Leo M. Gartland, during his life.'

all with the same force and effect as if this instrument had been delivered by him to said Trustee on May 16, 1931."

June 20, 1945, decedent sent a further document to the trustee which read in part:

> "SURRENDER BY LEO M. GARTLAND OF POWER OF APPOINTMENT UNDER TRUST AGREEMENT OF MATTHEW F. GARTLAND
>
> "Know All Men By These Presents:
>
> "That I do hereby finally and irrevocably renounce, release and surrender the Power of Appointment which is conferred upon me in and by Paragraph 8 of a Trust Agreement made by my father, the late Matthew F. Gartland, of Marion, Indiana, dated July 10th, 1929, over the trust fund for my benefit under said trust agreement.
>
> "It is my intent by this instrument to divest myself completely and irrevocably of all powers, rights and privileges granted to me by said trust agreement to dispose of, or to direct the disposition of, the principal or income of any part of the trust fund for my benefit under said trust agreement, as if such power of appointment had not been granted."

The decedent merely took the income from the trust for his life.

In seeking a reversal, the petitioner makes a threefold attack on the decision of the Tax Court. First, he contends that neither the decedent's letter of May 16, 1931, as ratified by the 1938 amendment, nor his release of his powers on June 20, 1945, constituted an "exercise" of a pre 1942 general power of appointment; secondly, that by virtue of the New York law which prohibited the accumulations of income except during the minority of a beneficiary, decedent's letter, as ratified by his amendment, was not an exercise of a general power of appointment; and finally, that even if it be assumed that any one or all of the three instruments constituted an "exercise" of a pre 1942 general power of appointment, such exercise did not make a

disposition of the type described in sections 2041(a)(1)(B) and 2036 (a)(1), Title 26 U.S.C.A.

The pertinent provisions of the 1954 Internal Revenue Code read in part:

> "§ 2041. Powers of appointment
>
> (a) In general.—The value of the gross estate shall include the value of all property . . . —
>
> (1) Powers of appointment created on or before October 21, 1942.—To the extent of any property with respect to which a general power of appointment created on or before October 21, 1942, is exercised by the decedent—
>
> (A) by will, or
>
> (B) by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate under sections 2035 to 2038, inclusive;
>
> but the failure to exercise such a power or the complete release of such a power shall not be deemed an exercise thereof. . . .
>
> • • •"
>
> "§ 2036. Transfers with retained life estate
>
> (a) General rule.—The value of the gross estate shall include the value of all property . . . to the extent of any interest therein of which the decedent has at any time made a transfer . . . by trust or otherwise, under which he has retained for his life or for any period not ascertainable without reference to his death or for any period which does not in fact end before his death—
>
> (1) the possession or enjoyment of, or the right to the income from, the property, or
>
> • • •"

In substance, petitioner's first contention is that the decedent did not exercise the general power of appointment provided by the terms of the trust agreement. By

the terms of the trust, the trustee was directed to pay the decedent only "so much of the income as the Trustee in his discretion shall deem advisable and to accumulate the remaining income and add it to the principal of the trust fund during the life of my said son." What possible right the decedent might have had under the terms of the trust and whether he exercised a general power of appointment must be determined under the applicable state law. *Estate of Rogers* v. *Commissioner*, 1943, 320 U.S. 410. At the time the trust was created, Matthew F. Gartland was domiciled in Indiana. By paragraph 12 of the trust, he selected the law of New Jersey to be applicable to the terms of the trust. The situs of the trust property after August 6, 1929 was in New York. It is immaterial which state law is applied. Decedent, by the terms of the trust, received only a hope or expectancy to receive the income from the corpus of the trust. *In re Uhl's Estate*, 7 Cir., (Ind.) 1957, 241 F. 2d 867, 869; *Herzog* v. *Commissioner of Internal Revenue*, 2 Cir., (N. Y.) 1941, 116 F. 2d 591, 593. See *Hardenburgh* v. *Blair*, 1879, 30 N.J. Eq. 645. In a suit by the decedent to force the trustee to pay him all the income without the letter of 1931 and the ratification of 1938, the trustee could have replied that he elected not to pay him. The Law of Trusts, Scott, 2d ed., 1956, Vol. 2, § 155, p. 1083; Handbook of the Law of Trust, Bogert, 2d ed., 1942, Ch. 4, § 46, pp. 166-7. Paragraph 8 of the trust authorized the decedent "to amend or terminate the agreement in whole or in part and to change any beneficial interest." There appears to be no dispute, nor could there be, that by this authority the decedent had a general power of appointment. The letter of 1931, ratified by the formal document of 1938, in which decedent employed the authority of paragraph 8, canceled the original provision in the agreement and in lieu thereof directed the trustee to pay de-

cedent the income "during his life." This amendment changed the decedent's hope or expectancy to receive the income, to a vested right to the income, whereby he could compel the trustee to pay him the income. Obviously, by the letter of 1931 and its ratification in 1938, decedent exercised his general power of appointment.

Petitioner argues that there was a lack of the necessary element of intent by the decedent to exercise the general power of appointment, either in the letter of 1931 or in the document of 1938, and that these writings reveal no words of appointment. Intent is an essential element to exercise a power of appointment in New York, Indiana and New Jersey. *In the Matter of Lucy Spitzmuller*, 1951, 279 App. Div. 233, 109 N.Y.S. 2d 1, Affirmed 304 N.Y. 608, 107 N.E. 2d 91; *Farnum* v. *The Pennsylvania Company for Insurance on Lives and Granting Annuities*, 1916, 87 N.J. Eq. 108, 99 Atl. 145, affirmed 87 N.J. Eq. 652, 101 Atl. 1053; *Bullerdick* v. *Wright*, 1897, 148 Ind. 477, 47 N.E. 931. In *Bullerdick* v. *Wright* the Court announced in 47 N.E. 931, 932-933:

> "The authorities uniformly affirm the doctrine that it is not essential to refer in express terms to the power, if an intention to execute it otherwise plainly appears; and any words or expressions indicating an intention to exercise the power will operate to that effect."

The decedent in his ratification of 1938 expressly referred to paragraph 8 of the trust, and indicated by his "words or expressions" an intention to exercise the general power of appointment.

Petitioner next urges that since the decedent was the real beneficiary of the trust, as evidenced by the power given him under paragraph 8 of the trust, the trustee would have given him the income if the decedent had

orally expressed a mere wish for it. As a matter of fact, paragraph 8 of the trust required "an instrument in writing" to exercise the power. Decedent exercised the power in writing, and it was after this that the trustee paid him the accumulated and current income.

Petitioner next argues that since the decedent did not attempt to control or change the disposition of the trust property at his death, he did not by the documents of 1931 and 1938 exercise his power of appointment. This argument is equally untenable. The exercise of a power of appointment is no less an exercise, because the decedent did not by the exercise control or change the disposition of the property at his death. Petitioner probably means by his argument that the exercise of a general power of appointment was not taxable, because he did not change the disposition of the trust property. Section 2041 imposes the tax upon the exercise of a pre 1942 general power of appointment and not upon the disposition of property by the exercise.

Prior to the 1942 amendment of the 1939 Internal Revenue Code (26 U.S.C.A. § 403, 1946 ed.), the statutes applicable to the exercise of a general power of appointment included the words "to the extent of any *property passing* under a general power of appointment." (Emphasis supplied.) The 1939 Internal Revenue Code (26 U.S.C.A. § 811, 1940 ed.), is typical and read in part:

> "§ 811. Gross estate
>
> "The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated . . .—
>
> • • •
>
> "(f) *Property passing* under general power of appointment. To the extent of any *property passing* under a general power of appointment exercised by

> the decedent (1) by will, or (2) by deed executed in contemplation of or intended to take effect in possession or enjoyment at or after his death, or (3) by deed under which he has retained for his life or any period not ascertainable without reference to his death or for any period which does not in fact end before his death (A) the possession or enjoyment of, or the right to the income from, the property, or. . . ." (Emphasis supplied.)

In *Helvering* v. *Grinnell*, 1934, 294 U.S. 153, the Supreme Court in construing a similar statute portrayed the importance of the words "property passing" when it said at p. 155:

> "The crucial words are 'property passing under a general power of appointment exercised by the decedent by will.' Analysis of this clause discloses three distinct requisites—(1) the existence of a general power of appointment; (2) an exercise of that power by the decedent by will; and (3) the passing of the property in virtue of such exercise."

This requirement of property passing was eliminated by the 1942 amendment of the Internal Revenue Code and was omitted from the 1951 Powers of Appointment Act, 26 U.S.C.A. § 811(f), 1954 Cumulative Annual Pocket Part, which in substance was the same as the present section 2041. Congress, by the omission of the words "property passing" from the statute, intended that a tax be imposed by section 2041, not upon the "property passing," but upon the exercise of the general power of appointment where it existed, regardless of whether property passed under the exercise of the power of appointment or whether there was a change in the disposition of the trust property at the death of the decedent. See *Keating* v. *Mayer*, 3 Cir., 1956, 236 F. 2d 478 and *Wilson* v. *Kraemer*, 2 Cir., 1951, 190 F. 2d 341, cert. denied 342 U.S. 859.

In discussing the 1951 Powers of Appointment Act, the Senate Committee Report clarified the intent and purpose of Congress in eliminating the requirement of passing of property by the exercise of a general power of appointment. Senate Report No. 382, 82nd Congress, 1st Sess., 2 U.S. Code, Congressional and Administrative News, 1951, pp. 1530, 1531-1532, reads in part:

> "Section 1 of the bill amends section 811(f) of the code, relating to estate tax on powers of appointment. The new section 811(f)(1) deals with preexisting powers, *i.e.*, powers created on or before October 21, 1942, the date of enactment of the 1942 act. As to such powers it restores the situation which existed prior to that date, *i.e.*, only the exercise of a general power of appointment is taxed. An amendment by your committee makes it clear that a complete release of a preexisting power at any time is not taxable.
>
> "The former statute taxed property 'passing' under a general power of appointment exercised by the decedent. This sometimes gave rise to litigation where the decedent appointed part or all of the property to persons who would also have taken it under the terms of the original instrument creating the power. The bill eliminates this possibility by taxing all property with respect to which the decedent has 'exercised' a general power of appointment.
>
> "With this exception, the intent of the bill is to restore the law regarding preexisting powers as it existed prior to the 1942 act."

In determining the taxability of the exercise of a general power of appointment, the federal law and not the state law is applicable. *Estate of Rogers* v. *Commissioner, supra.* Congress intended that the tax be imposed upon "all the property [in the trust estate] with respect to which the decedent has exercised a general power of appointment." In the instant case the decedent exercised his power of

appointment, and it is immaterial so far as the "exercise" is concerned that no change was made in the remaindermen as provided by the trust agreement.

Petitioner next contends that the decedent did not exercise his power of appointment because his letter of 1931 and the ratification of 1938 to take the income were a nullity, since under the New York Statute, the trustee could not accumulate income and was required to pay the income to the decedent. Prior to September 1, 1959, section 16 of the New York Personal Property Law provided as follows:

> "An accumulation of the income of personal property, directed by any instrument sufficient in law to pass such property is valid:
>
> "1. If directed to commence from the date of the instrument, or the death of the person executing the same, and to be made for the benefit of one or more minors then in being, or in being at such death, and to terminate at or before the expiration of their minority.
>
> "2. If directed to commence at any period subsequent to the date of the instrument or subsequent to the death of the person executing it, and directed to commence within the time allowed for the suspension of the absolute ownership of personal property, and at some time during the minority of the persons for whose benefit it is intended, and to terminate at or before the expiration of their minority.
>
> "3. All other directions for the accumulation of the income of personal property, not authorized by statute, are void. In either case mentioned in subdivisions one and two of this section a direction for any such accumulation for a longer term than the minority of the persons intended to be benefited thereby, has the same effect as if limited to the minority of such persons, and is void as respects the time beyond such minority." Personal Property Law, Vol. 40, section 16, McKinneys Consolidated Laws of

New York, Annotated, 1949. Repealed N.Y. Sess. Laws 1959, c. 453 § 1, 4, effective September 1, 1959.

(Burns Ind. Stat. Annotated, 1933, section 51-102 contains, in effect, a similar statute.) Petitioner again construes the original trust agreement to mean that Leo M. Gartland was entitled to the income from the trust property during his life. As has already been set forth, the decedent did not have the right to the income until he exercised his power of appointment. Since Leo M. Gartland was born in 1895 and married in 1919, as disclosed by the Federal estate tax return, it is reasonable to infer that his children were minors in 1931. Assuming the provision for the accumulations of income was invalidated by the New York Statute, it does not follow that Leo M. Gartland, who could only receive the income at the discretion of the trustee, would have been entitled to this income. The accumulated income would have been paid to the person or persons presumptively entitled to the next eventual estate. *In Re Berthet's Estate*, 1959, 196 N.Y.S. 2d 354; *In Re Roeser's Will*, 1956, 155 N.Y.S. 2d 108; *In Re Ball's Will*, 1940, 24 N.Y.S. 2d 432; *Central Union Trust Co.* v. *Trimble*, 1930, 255 N.Y. 88; *St. John* v. *Andrews Institute for Girls*, 1908, 191 N.Y. 254, 83 N.E. 981. It must be concluded that even if the provision for the accumulations of income was void by virtue of the New York Statute, the decedent did and was required to exercise the general power of appointment to obtain the income from the trust property during his life.

Petitioner further claims that the 1945 release executed by decedent avoided the tax under section 2041(a)(1)(B). Treasury Estate Tax Regulation 1954 Code, 26 CFR § 20.2041-2(d), 1961 reads:

> "If, at or before the time a power of appointment is relinquished, the holder of the power exercises the

power in such a manner or to such an extent that the relinquishment results in the reduction, enlargement, or shift in a beneficial interest in property, the relinquishment will be considered to be an exercise and not a release of the power."

Clearly, the release executed in 1945 by the decedent was not a complete release, as required by section 2041(a)(1)(B), of his power of appointment, because before the execution of the release, he had taken a life estate which shifted the "beneficial interest" in the trust property from the manner in which it was to be distributed by the terms of the original trust agreement.

This brings forward petitioner's final contention that even if the decedent's three documents of 1931, 1938 and 1945 did constitute an exercise of a pre 1942 general power of appointment, such exercise was not a disposition of the trust property of the type described in section 2041(a)(1)(B) and section 2036(a)(1). It must be kept in mind, in determining this issue, that section 2041(a)(1)(B) imposes a tax upon the exercise of a pre 1932 power of appointment by including in the gross estate the entire value of the trust property regardless of whether property passed by virtue of the exercise, where the power existed in the decedent by the terms of the trust, and was exercised in a manner prescribed by section 2041(a)(1)(B) and section 2036(a)(1). Reading sections 2041(a)(1)(B) and 2036(a)(1) together, to determine whether a general power of appointment is exercised in the prescribed manner, the applicable wording of these statutes is (§ 2041(a)(1)(B)) "a disposition which is of such a nature that if it were a transfer of property owned by the decedent, such property would be includible in decedent's gross estate" such as (§ 2036(a)(1)) "a transfer . . . by trust or otherwise, under which he has retained for his life . . . (1) . . .

the right to the income from, the property. . . ." In referring to the transfer of property we find that section 2041(a)(1)(B) requires only a disposition which is of such a nature that if it were a transfer and not a transfer as required by section 2036(a)(1) such property would be includible in decedent's gross estate. Thus, for tax purposes under section 2036(a)(1), a decedent is required to make an actual transfer of the trust property, retaining the life income, but under section 2041(a)(1)(B) a decedent is not required to make an actual transfer. It also must be noted that section 2041(a)(1)(B) does not refer to a transfer of property owned by the decedent but to a transfer of property as if it were owned by the decedent. Section 2041(a)(1)(B) speaks of a general power of appointment for tax purposes as if the decedent owned the property. The remainders over, under the terms of the trust agreement, existed subject to being divested by the exercise of the general power of appointment. In effect, when decedent took only the life estate, considering that he was the owner of the corpus of the trust, he vested in or transferred, by trust or otherwise, the corpus of the trust to the remaindermen, provided he made no further exercise of his general power of appointment. In other words, by the taking of the life estate in the corpus of the trust, a decedent makes a disposition of such a nature whereby he transfers the property by trust or otherwise, retaining a life income. When the decedent, in the instant case, released the power of appointment in 1945, after taking the income, he caused the remainders to become vested at that time, but did not change the nature of the transfer or disposition of the trust property. This Court concludes, therefore, that the exercise of the power of appointment by Leo M. Gartland effectuated the type of transfer or disposition which is described and required by section 2041(a)(1)(B). See

Lee v. *Commissioner of Internal Revenue*, C.A.D.C., 1932, 57 F. 2d 399; *Wear* v. *Commissioner of Internal Revenue*, 3 Cir., 1933, 65 F. 2d 665. Both *Wear* and *Lee* were decided under the applicable statute prior to 1942, and were overruled in *Helvering* v. *Grinnell*, *supra*, due to the requirement in the statute of "property passing under a general power of appointment." This Court believes that these cases would not have been overruled had the present wording of the statute been in effect. *Helvering* v. *Grinnell*, *supra*, is no longer decisive under the present wording of the statute. As was said in the Senate Report previously referred to, "[w]ith this exception [of property passing] the intent of the bill is to restore the law regarding pre-existing powers as it existed prior to the 1942 act." In determining whether the transfer or disposition in the instant case was a transfer or disposition of the type required by the present statute, consideration must be given to the intent of Congress to tax the exercise of the power of appointment although no property actually passed by the exercise. This solution of the issue is borne out by the example given in Treasury Estate Tax Regulation, 1954 Code, 26 CFR § 20.2041-2(c), 1961 which reads:

> "Example (2). S created a trust in 1930 to pay the income to A for life, remainder as B appoints by an instrument filed with the trustee during B's lifetime, and in default of appointment remainder to C. B exercised the power in 1955 by directing that after A's death the income be paid to himself for life with remainder to C. If B dies after A, the entire value of the trust property would be included in B's gross estate, since such a disposition if it were a transfer of property owned by B would cause the property to be included in his gross estate under section 2036(a)(1). If B dies before A, the value of the trust property less the value of A's life estate would be included in B's gross estate for the same reason."

The petitioner has cited *Estate of Bernard E. Denzer*, 1957, 29 T.C. 237, in support of his position that by taking the life estate there was no transfer of the property under section 2041(a)(1)(B). In that case, the question was whether one-half of the trust property was included in the decedent's estate by section 811(c)(1)(B), 26 U.S.C.A., 1954 Cumulative Annual Pocket Part (1951 Act), which is now section 2036. Moreover, the facts in that case disclose that the son of the Settlor had a life estate in the trust property and there was neither an actual transfer of this trust property nor the reservation of a life estate.

In accordance with the views expressed, this Court holds that the Tax Court properly included in the decedent's gross estate the value of the entire corpus of the trust created by Matthew F. Gartland. The decision of the Tax Court is AFFIRMED.

A true Copy:
Teste:

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Clerk of the United States Court of
Appeals for the Seventh Circuit.